

STATE OF ILLINOIS
ILLINOIS COMMERCE COMMISSION

Illinois Commerce Commission
On its Own Motion

-vs-

Northern Illinois Gas Company
d/b/a Nicor Gas Company

Reconciliation of revenues collected
under gas adjustment charges with
actual costs prudently incurred.

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Docket No. 03-0703
on Rehearing

REPLY BRIEF ON REHEARING OF THE STAFF
OF THE ILLINOIS COMMERCE COMMISSION

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Staff of the Illinois Commerce Commission (“Staff”), by and through its counsel, pursuant to Section 200.800 of the Rules of Practice (83 Ill. Adm. Code 200.800) of the Illinois Commerce Commission (“Commission”), respectfully submits its Reply Brief on Rehearing (“RB on Rehearing”) in the above-captioned matter.

I. INTRODUCTION

A. Procedural Background

Staff’s Initial Brief on Rehearing (“IB on Rehearing”) was filed and served on Northern Illinois Gas Company d/b/a Nicor Gas (“Nicor” or “Company” or “Nicor Gas”), the Citizens Utility Board (“CUB”), the People of the State of Illinois by Attorney General Lisa Madigan (“AG”) and the Administrative Law Judge (“ALJ”) on January 11, 2016. The Company, CUB and AG (collectively “CUB-AG”) also filed and served their IB on Rehearing in this matter on the same day. Many of the issues raised in Nicor’s IB on Rehearing and CUB-AG’s IB on Rehearing were addressed in Staff’s IB on Rehearing. The absence of a

response to a specific issue raised in Nicor's IB on Rehearing or CUB-AG's IB on Rehearing does not constitute a change of position from the Staff IB on Rehearing or other previously filed briefs. Staff's RB on Rehearing follows.

B. Scope of Rehearing

As addressed in Staff's IB on Rehearing, Staff, Nicor, CUB and AG agree that the scope of rehearing encompassed all that was set forth in the CUB application for rehearing. (Tr. 6:4-7, December 3, 2015.) The CUB application for rehearing was very broad. CUB requested that the Commission reconsider and rehear the proceeding. (CUB Application for Rehearing, 7.) In its application for rehearing, CUB alleged certain errors by the Commission. CUB alleged that the Commission:

- (1) ignored and arbitrarily rejected record evidence demonstrating the unreasonableness of Nicor's use of stored gas for third parties during the reconciliation year;
- (2) misapplied the prudence standard; and
- (3) erroneously accepted Nicor's claim that CUB and Staff's¹ adjustments are based upon hindsight review.

(Id. at 1 and 6.)

C. Legal Standards

As set forth in Staff's IB on Rehearing, Initial Brief ("IB") and Reply Brief ("RB"), the relevant statute is Section 9-220 of the Public Utilities Act ("PUA"). Section 9-220 of the PUA provides that the Commission may authorize an increase or decrease in rates and

¹ While the CUB-AG Application for Rehearing does not specifically refer to Staff's adjustment, the portion of the final order with which CUB-AG takes issue indicates that the Commission found not just CUB's but also Staff's adjustment to be improper hindsight review. (CUB-AG Application for Rehearing, 6.)

charges based upon changes in the cost of purchased gas through the application of a purchased gas adjustment clause. Section 9-220(a) requires the Commission to initiate annual public hearings to:

determine whether the clauses reflect actual costs of fuel, gas, power, or coal transportation purchased to determine whether such purchases were prudent, and to reconcile any amounts collected with the actual costs of fuel, power, gas, or coal transportation prudently purchased. In each such proceeding, the burden of proof shall be upon the utility to establish the prudence of its cost of fuel, power, gas, or coal transportation purchases and costs. ...

(220 ILCS 5/9-220(a).)

The relevant Commission rules are found at 83 Ill. Adm. Code 525, "Uniform Purchased Gas Adjustment Clause" ("Part 525"). For gas purchases, the provisions of Section 9-220 of the PUA are implemented by Part 525. Section 525.40 of Part 525 identifies gas costs that are recoverable through a PGA. Adjustments to gas costs through the Adjustment Factor are addressed in Section 525.50. The gas charge formula is contained in Section 525.60. Annual reconciliation procedures are described in Section 525.70.

The Commission has defined prudence as:

[...] that standard of care which a reasonable person would be expected to exercise under the circumstances encountered by utility management at the time decisions had to be made. In determining whether or not a judgment was prudently made, only those facts available at the time the judgment was exercised can be considered. Hindsight review is impermissible. Imprudence cannot be sustained by substituting one's judgment for that of another. The prudence standard recognizes that reasonable persons can have honest differences of opinion without one or the other necessarily being 'imprudent'.

(Order, Docket No. 84-0395, October 7, 1987, p. 17)

Also, in Docket No. 88-0142, the Commission defined prudence as follows:

Prudence is that standard of care which a reasonable person would be expected to exercise under the same circumstances encountered by utility

management at the time decisions had to be made. In determining whether a judgment was prudently made, only those facts available at the time judgment was exercised can be considered. Hindsight review is impermissible.

(Order, Docket No. 88-0142, February 5, 1992, pp. 25-26)

In Section 9-220(a) proceedings, the burden of proof is on Nicor Gas to establish the prudence of its costs of gas purchases and related costs. (220 ILCS 5/9-220(a)). Nicor Gas has the burden to prove the prudence of these costs by a preponderance of the evidence. (5 ILCS 100/10-15). Preponderance of the evidence has been defined as the evidence that is more probably true than not. (See, e.g., Witherell v. Weimer, 118 Ill. 2d, 321, 336, 515 N.E.2d 68 (1987)).

II. ARGUMENT - RESPONSE TO NICOR

A. Record Evidence Shows that Nicor Gas Was Imprudent

Nicor argues in support of the Commission's conclusion in its September 16, 2015 final order that Staff and CUB failed to provide substantive evidence that demonstrates that Nicor's gas supply purchases and costs were imprudent or improper. (Nicor IB on Rehearing, 5.) The Commission should reject Nicor's arguments and reverse its conclusion in its September 16, 2015 Final Order. As Staff made clear in its IB on Rehearing, Staff witness Dr. Rearden's second adjustment represents the increase in gas costs above the revenues Nicor earned from providing Hub services. (Staff IB on Rehearing, 6.) Whether Nicor's provision of Hub services was prudent or not depended on a comparison of the revenues earned for the services to the cost of supplying the services. (Id., 7.) The evidence in the record showed that Nicor Gas made no attempt whatsoever to analyze whether any individual Hub services revenues exceeded the costs of providing those services. Rather, Nicor Gas simply assumed, without conducting any analysis, that it incurred no costs as a result of the Hub loans. (Id.) Because Nicor made

no attempt whatsoever to determine whether the expected cost of the loan was less than the revenue generated by the loan, which was the only way it could be deemed prudent, Nicor operated the Hub with no regard for whether the transactions were prudent. Despite Nicor's claims to the contrary, the evidence supports a finding of imprudence on Nicor Gas' part.

B. Nicor Gas' Hub Activities Did Impact Gas Withdrawals for PGA Customers in 2003

Nicor argues that Nicor's Hub services did not impact the gas that was available to PGA customers in 2003. (Nicor IB on Rehearing, 5.) Nicor argues that the gas Nicor withdrew in February and March 2003 was previously stored in Nicor Gas' storage fields by third parties and was not associated with Nicor Gas' PGA customers. (Nicor Gas IB on Rehearing, 6.) Staff addressed this issue in its RB. Despite Nicor Gas' claims to the contrary, the gas stored for transportation customers was not used to support the loans. (Staff Ex. 4.0 (Public), 4:70-79.)

To support the loans, Nicor would have had to use gas otherwise purchased for ratepayers. (Id., 4:75-79.) (Staff RB, 13.) Since Nicor did not have title to transportation customers' gas stored in their banks, those volumes could not be the source for the loans. (Staff Ex. 4.0 (Public), 9.) Also, Nicor could not loan Hub customers' gas, because Nicor loaned more gas to Hub customers than Hub customers injected into storage. (Staff RB, 13.)

In addition, and relatedly, supplying the Hub loans necessarily involved assets and services for which costs are recovered in the PGA through displacement. Displacement means that in the process of balancing its system, Nicor is using assets, such as pipeline

transportation and storage and purchased gas, to balance the system amongst all customers. Thus, Nicor Gas incurs PGA recoverable costs to supply Hub customers with loans. (Staff IB, 8.)

C. The Commission Should Reject Nicor's Claim that Hub Loans Were Necessary to Cycle the Storage Fields.

Nicor Gas argues that its Hub services provided the necessary cycling of stored gas for its aquifer storage fields and that the Commission appropriately accepted Nicor's explanation that Hub services were necessary. (Nicor IB on Rehearing 7-8.) While aquifer storage fields must be sufficiently filled and emptied each year (i.e. cycled) (Tr., 174:5, March 17, 2015), the Hub transactions were not required to empty the storage fields. Dr. Rearden testified that Nicor could have cut back on non-firm purchases and delivered more stored gas to sales customers rather than deliver it to Hub customers. (Staff Ex. 4.0 (Public), 9:187-189.) As Staff addressed in its RB, Dr. Rearden provided evidence that Nicor planned to use storage capacity for Hub loans rather than to supply ratepayers. Nicor offers no explanation why it could not have planned to use that capacity and gas to supply sales customers. (Staff Ex. 4.0 (Public), 9:182-10:207; 8:165-175.) (Staff RB, 12.)

D. Staff Did Not Engage in Improper Hindsight Review

Nicor argues that the Commission correctly concluded that Staff's and CUB's witnesses engaged in impermissible hindsight review when they challenged Nicor actions based entirely on information available only after the reconciliation period in question. (Nicor Gas IB on Rehearing, 11.) Nicor argues that Staff's and CUB's damage

calculations are based upon pricing information not available to Nicor Gas at the time it entered into its loan agreements. (Id., 12.) However, as Staff showed in its IB on Rehearing, the CUB-AG and Staff adjustments are not based on hindsight. In other words, Staff and CUB-AG use the market price of gas not to determine whether Nicor's conduct was imprudent, but rather as a measure of damages, to determine what Nicor's demonstrated imprudence cost ratepayers. (See CUB-AG Application for Rehearing, 6.) The principle of hindsight review is only relevant to the question of whether a judgment was prudently made.

Nicor's imprudent decision at issue here was the decision that there was no cost for the Hub transactions. Staff simply used the same facts that were available to the Company at the time it made its decision, to determine whether the Nicor decision was imprudent. As discussed above, when Nicor concluded that Hub transactions had no cost, Nicor failed to perform any analysis of the expected revenue from its Hub transactions compared to the expected cost of each transaction. That decision by Nicor ultimately results in Nicor being unable to meet its burden of showing that the Hub transactions were prudent. (Staff IB on Rehearing, 9.)

III. CONCLUSION

Staff respectfully requests that the Illinois Commerce Commission approve Staff's recommendations in this docket.

Respectfully submitted,

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